



Governor C.L. “Butch” Otter Budget Recommendation

FY 2012 & FY 2013

January 10, 2012

Wayne L. Hammon, DFM Administrator

Good morning.

My name is Wayne Hammon and I am the Administrator of the Idaho Division of Financial Management, the State’s central budget office within the Executive branch. On behalf of Idaho Governor C.L. “Butch” Otter, it is my honor to welcome you back to the Capitol and extend to you his sincere best wishes as you begin your task of setting the state budget.

With me today are members of my staff. It is my hope that you will get to know each of them better over the coming months as you complete your work. Along with the LSO budget and policy staff, my team of analysts work hard all year to develop the budget expertise necessary to ensure the proper management of our limited state resources. I and each of them are available to you at moments notice and I encourage you to call upon them whenever we might be of assistance.

Outline

- Revenues & Updated Forecast
- FY 2012
 - Grocery Tax Credit
 - Supplementals & Deficiency Warrants
- FY 2013
 - Transfers to and from General Fund
 - Budget Priorities
 - Tax Relief
- Summaries & Ending Balances



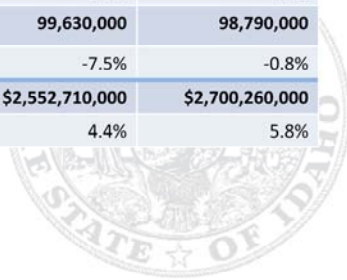
Today I want to cover in broad brush strokes the goals and priorities outlined in the Governor's FY 2013 budget recommendation.

The details of the Governor's recommendation have been incorporated into your JFAC Budget Books and will be addressed by members of the Governor's cabinet as they appear before you over the next several weeks. In our time together today, I want to hit the highlights and answer as many of your questions as possible.

We will begin by discussing the updated revenue forecast which was released just yesterday. This will serve as our starting point for our discussion of spending recommendations for the remainder of the current fiscal year and for next year. We will conclude with a quick summary and a look at the updated projected ending balances.

Revenues

| | FY 2010 | FY 2011 | FY 2012 | FY 2013 |
|--------------------|-----------------|-----------------|-----------------|-----------------|
| Individual Income | \$1,061,880,000 | \$1,152,650,000 | \$1,216,760,000 | \$1,295,000,000 |
| % Change | -9.1% | 8.5% | 5.8% | 6.2% |
| Corporate Income | 97,020,000 | 168,950,000 | 176,760,000 | 182,840,000 |
| % Change | -31.2% | 74.1% | 4.6% | 3.4% |
| Sales Tax | 955,910,000 | 972,380,000 | 1,013,400,000 | 1,082,720,000 |
| % Change | -6.5% | 1.7% | 4.2% | 6.8% |
| Product Taxes | 41,180,000 | 42,820,000 | 43,160,000 | 40,910,000 |
| % Change | 38.5% | 4.0% | 0.8% | -5.2% |
| Misc. Revenue | 108,470,000 | 107,680,000 | 99,630,000 | 98,790,000 |
| % Change | 3.6% | -0.7% | -7.5% | -0.8% |
| Total General Fund | \$2,264,460,000 | \$2,444,470,000 | \$2,552,710,000 | \$2,700,260,000 |
| % Change | -8.2% | 7.9% | 4.4% | 5.8% |



I am pleased to have with me today Idaho's Chief Economist Derek Santos. Mr. Santos has over 25 years of experience with Idaho's economy and I believe you will come to the same conclusion that I have that nobody understands the complex nature of our economy and the state's revenue stream better than he does.

Yesterday as part of his State of State and Budget Address, the Governor announced Mr. Santos' newest revenue forecast which is represented in this table. The two years left of the blue line are actual collections, the two to the right are forecasts. The updated forecast calls for growth in the General Fund at 4.4 percent for the current fiscal year and 5.8 percent next year.

While significantly less than the earlier forecasts, these updated growth projections show continued strengthening of the economy and reflect increased economic activity in a most sectors of Idaho's economy.

For comparison sake, a General Fund revenue target of \$2.5 million is comparable to the returns the State realized in fiscal year 2006.

Revenues – December Collections



The updated revenue forecast was based upon the best economic data available in mid-December 2011. It also reflects actual tax collections through November 2011.

This chart shows the State's General Fund revenue collections for the month of December. These figures were not included in the analysis of the new revenue forecast.

Revenues – Year-to-Date



This chart shows revenue collection measured against the updated forecast through the first six months of the current fiscal year.

FY 2012

- Transfers to and from the General Fund
 - Grocery Tax Credit
 - Section 63-3024A, Idaho Code, provides:
 - Tax credit against taxes due
 - Annual increases in the credit amounts
 - A “trigger” for delaying the annual increases when necessary
 - The Governor recommended and the Legislature concurred to delay the increase scheduled for the tax year 2011
 - HCR 25 (adopted 55-10-5 in House and 29-5-1 in Senate)
 - Financial picture has changed and Governor did not issue the Executive Order required to exercise the trigger
 - Results in \$15 million decrease in General Fund Revenue



When it comes to our discussion of the current fiscal year, the first area I wish to address is the Grocery Tax Credit.

As you are aware, during last year’s legislative session, the Governor recommended, this committee approved, and the entire legislature agreed to delay for one year the next phase of the grocery tax credit. Having ended FY 2011 with more revenues than had been projected, the Governor determined that this delay was not necessary and did not issue the executive order authorized in HCR 25.

As a result, the expansion of the tax credit was not delayed and \$15 million in tax relief has been delivered to the citizens of Idaho.

No further action is required by the legislature on this issue.

FY 2012

- Deficiency Warrants

| | |
|----------------------------------|--------------|
| – Lands – fire suppression | \$ 4,093,300 |
| – Military – hazardous materials | \$ 69,800 |
| – Agriculture – invasive species | \$ 58,200 |

- General Fund Supplementals

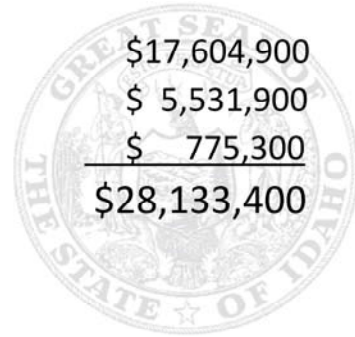
| | |
|----------------------|--------------|
| – CAT Fund | \$17,604,900 |
| – Health and Welfare | \$ 5,531,900 |
| – Other Agencies | \$ 775,300 |

- Total

\$28,133,400



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As I am sure you already know, the Governor and his cabinet are very careful in their exercise of the authority to issue deficiency warrants. Every effort has been made to capture reimbursement from our partners including the federal government and, when it comes to hazardous material abatement, the private property owners responsible for the incidents. As the chair of the Board of Examiners' subcommittee that monitors these deficiency warrants, I can report to you that the Office of the Attorney General has been a tremendous partner in our efforts to capture reimbursement from every possible source and thus reduce the dollar amount of the deficiency warrants.

Again this year, the staff at DFM has worked with agency directors and the LSO budget and policy staff to reduce the number and size of supplemental appropriations to those that are truly necessary. Spending that can be delayed until the start of the fiscal year has not been recommended as a supplemental and wherever possible existing agency resources have been redirected to cover the need identified in the agencies' request.

Nonetheless, there remains a number of supplementals in the Governor's recommendation. These include \$23.9 from the General Fund. As you might expect, the bulk of this spending is within the health and human services area, more specifically in the CAT Fund and the Department of Health and Welfare. These two items account for 97 percent of supplemental spending.

That concludes the areas of concern for the current fiscal year. We will see these figures again when we look at the recommendation's summary at the end of my presentation.

FY 2013

- Changes from prior year
 - Governor's recommendation includes statutory BSF Transfer (\$9,456,200)
 - Governor's recommendation includes next phase of the Grocery Tax Credit (\$15,532,300)
 - 5 percent cap on overall General Fund growth
- Three-tiered approach to new spending:
 - Tier 1 = Governor's Priorities
 - Tier 2 = Strategic Investments
 - Tier 3 = Agency Initiatives



Turning to the current fiscal year there are a couple of changes I want to draw to your attention.

First, the Governor's recommendation accounts for the statutory transfer to the budget stabilization fund. Unlike last year, we are not asking you to consider waiving this statutory requirement.

Second, the Governor's recommendation accounts for the scheduled increase in the grocery tax credit. Allowing this already authorized change to take affect will provide Idaho families another \$15.5 million in much needed tax relief.

Third, the Governor's recommendation limits growth in General Fund spending to no more than 5 percent of the FY 2012 appropriations.

In order to understand how the decisions reflected in the Governor's recommendation were reached, I believe we must first consider the framework by which all agency requests were considered. The Governor has outlined a three-tiered approach to all new spending.

First, he has outlined a limited number of priorities that he believes must be addressed. We will cover each of these in detail today. Second, he identified a handful of strategic investments that while they do cost money, will provide tremendous return to the State over the long-term. Finally, other requests made by the agencies were considered and those initiatives highest in priority are included in the recommendation. Spending in this third tier was limited by the Governor to no more than two percent growth. This two percent cap was applied to both General Fund spending as well as the growth in the agency's total fund appropriation.

FY 2013

- Tier 1 = Governor's Priorities

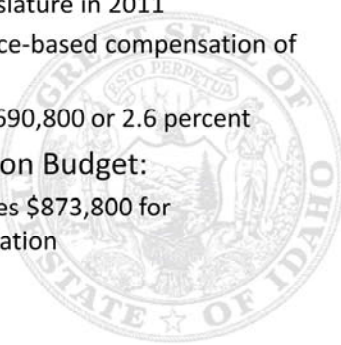
- Priority #1 = Education

- K-12 Budget:

- Governor's recommendation fully funds the "Students Come First" changes approved by the Legislature in 2011
 - » Includes funding for performance-based compensation of teachers and administrators
 - Total General Fund increase of \$31,690,800 or 2.6 percent

- Superintendent of Public Instruction Budget:

- Governor's recommendation includes \$873,800 for longitudinal data system implementation



As you will recall, the Governor laid out his priorities very early when he stated that any new revenue must first be devoted to education. As a result, public schools support receives the lion's share of new funding in the Governor's recommendation – second only to Medicaid. The Governor's recommendation fully funds the Students Come First changes approved last year by the Legislature and other essential priorities outlined by Superintendent of Public Instruction Tom Luna.

FY 2013

- Tier 1 = Governor's Priorities
 - Priority #1 = Education
 - Higher Education Budget:
 - Governor's recommendation fully funds FY 2013 Enrollment Workload Adjustment (EWA) and Occupancy Costs
 - » Included for Colleges and Universities, Community Colleges, Professional-Technical Education, and Agricultural Research and Extension
 - » Highest priority item for institutions
 - » First time these maintenance items have been funded since FY 2009
 - Governor's recommendation includes creation of IGEM – the Idaho Global Entrepreneurial Mission



The Governor's focus on education also accounts for pressing needs in the higher education budget.

For the first time in four years, the Governor's recommendation includes funding for Enrollment Workload Adjustments and Occupancy Costs for both the four state institutions of higher education as well as our community colleges and other higher education budgets.

Just as significant is the Governor's commitment to the Idaho Global Entrepreneurial Mission – or IGEM.

IGEM

- IGEM's mission is to create new enterprises and high-paying knowledge-based economy jobs by increasing strategic areas of research and development through targeted partnerships among industry, higher education and government that leverage new and existing resources.
- Strategies:
 - Invest in strategic research
 - Attract outstanding innovators in areas of strength and opportunity
 - Increase research funding
 - Invest in entrepreneurial ecosystem

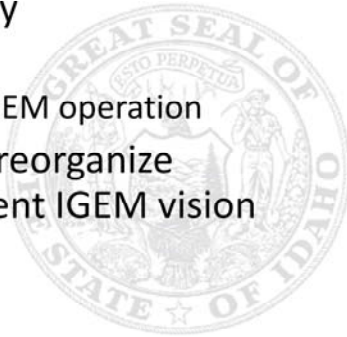


IGEM is a comprehensive strategy to enable Idaho's stakeholders to collaborate and leverage resources with the goal of increasing the state's knowledge-based economy.

Successful implementation of IGEM strategies will increase the research capacity of Idaho's universities in strategic areas, develop a world-class talent pool, and develop dynamic consortium of industry, university and government partnerships. These economic drivers will generate globally competitive technologies, high-paying jobs, new startups and an expanded tax base.

IGEM

- Center for Advance Energy Studies (CAES)
 - \$2 million
- New Research initiatives at Universities
 - \$2 million
- Partnership with private industry
 - \$1 million
 - Includes funding for grants and IGEM operation
- Legislation being introduced to reorganize Innovation Council and implement IGEM vision



So what does that mean for you, the Joint Finance and Appropriations Committee?

The Governor's recommendation includes \$5 million in ongoing General Fund appropriations in these three areas:

\$2 million for CAES

\$2 million for new research

\$1 million for the IGEM operation and to fund bridge financing to bring the ideas developed in our state institutions of higher education to the market place

Also, the Governor's office will be introducing legislation to change how these funds are administered.

FY 2013

- Tier 1 = Governor's Priorities
 - Priority #2 – Create Jobs and Advance Economic Development
 - IGEM
 - \$5 million
 - Department of Commerce grants
 - \$750,000
 - Tax Relief
 - \$45 million



The Governor's second priority is to create jobs and advance economic development.

Of course, IGEM will play an important role in fulfilling the Governor's vision in this area. As will restoring the economic development grants at the Department of Commerce that have been eroded during our recent economic downturn.

Just as important is the need to provide tax relief to the Idaho economy.

As the Governor pointed out yesterday, he has engaged legislators, business groups and other stakeholders on what the tax relief package should look like. While there is not yet consensus on what the form of the tax relief should take, there is consensus on the need for reducing the tax burden for both individual taxpayers and the employers which drive our economy.

FY 2013

- Tier 1 = Governor's Priorities
 - Priority #3 – State Rainy Day Funds
 - Statutory BSF transfer \$ 9,456,200
 - Additional transfers \$50,543,800
 - Distributed between funds based upon share of the overall General Fund budget
 - BSF \$16,523,800
 - PESF \$29,040,000
 - HESF \$ 4,980,000
 - Total transfer to rainy day funds \$60,000,000



The third priority captured in the Governor's recommendation is to begin the process of restoring the State's rainy day accounts.

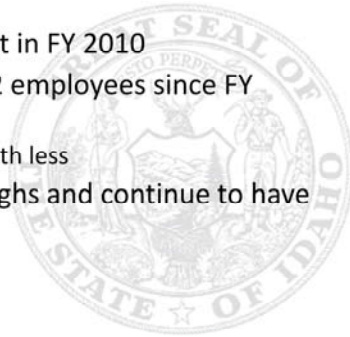
As each of you are aware, Idaho had almost \$400 million in our rainy day accounts on at the end of FY 2008. Those accounts now total less than \$30 million. As painful as the last four years have been, we can all agree that it would have been even worse had we not started from a position of strength.

The time to start saving for the next rainy day is today.

The Governor's recommendation includes a total of \$60 million in transfers to the State's three main rainy day accounts. These amounts divide transfers to the Budget Stabilization Fund, Public Education Stabilization Fund, and the Higher Education Stabilization Fund according to their representative share of the FY 2012 General Fund appropriations.

FY 2013

- Tier 1 = Governor's Priorities
 - Priority #4 – State Employees
 - There has been no CEC for state employees since FY 2009
 - Much of this General Fund increase was returned in response to the mid-year holdback ordered by the Governor and expanded by the Legislature
 - All agencies experienced a 5% PC cut in FY 2010
 - State workforce has shrunk by 1,912 employees since FY 2008
 - Those that remain are doing more with less
 - Many agencies have endured furloughs and continue to have large number of vacancies



The fourth priority in tier one is our hard working state employees. I need not remind you that our state workforce has been doing more with less during the past four years.

FY 2013

- Tier 1 = Governor's Priorities

- Priority #4 – State Employees

- Recommendation includes the statutory changes for elected officials (ongoing)
 - Recommendation also includes setting aside funds equal to a merit based 3 percent CEC in all agencies and across all funds (one-time) including public schools
 - To be delivered should revenues meet forecast expectations
 - Agency directors to be given flexibility to apply funds to most critical areas within their responsibility
 - \$41.1 million in General Fund (\$17.2 other fund sources)



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To address this need, the Governor's recommendation includes a one-time surplus eliminator in the amount equivalent to a merit based 3 percent CEC in all agencies across all fund sources including public schools.

Obviously this is not the ideal situation we find ourselves in. The Governor very much wanted to be able to recommend on-going salary adjustments. However, as we have learned over the past few years it is better to be cautious when so much uncertainty remains. I would hate to put anyone in the position of rewarding employees with a raise and then telling them a month or two later that they now have to take furloughs to pay for it.

The Governor has proposed that these funds be released in two stages. The first half would be released in July 2012 at the start of fiscal year 2013 provided the State finishes the current fiscal year inline with the new updated revenue forecast discussed earlier. The second half would be released at the mid-year point, or January 2013, should revenues over the first six months of fiscal year 2013 continue to track with projections and the budget established by this committee over the next couple of months. Of course, the Governor is open to working with this committee to refine these triggers and welcomes your ideas.

FY 2013

- Tier 1 = Governor's Priorities

- Priority #4 – State Employees

- Governor's recommendation also fully funds changes in employee benefits
 - Increase health insurance costs
 - New employee wellness program
 - No change in PERSI rate
 - Total of \$12.5 million in General Fund (\$16.6 million from other fund sources) for state employee benefits



Finally, there are other things we can do for our state employees.

The Governor's recommendation includes fully funding the costs associated with changes in employee benefits. Failure to approve this funding would have a direct impact on employee take-home pay.

FY 2013

- Tiers 2 & 3 = Strategic Investments and Agency Initiatives
 - Includes modest amounts for:
 - Replacement capitol (non General Fund)
 - Inflation (non General Fund)
 - Limited line items
- Overall General Fund increase in spending limited to 5 percent

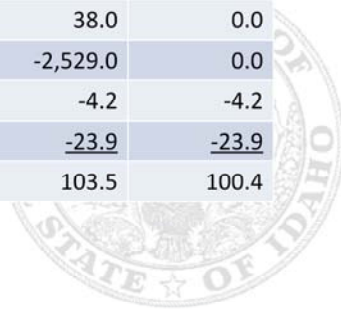


The rest of the spending included in the Governor's recommendation falls into tiers 2 and 3. These line items have been evaluated to ensure that highest priority among them are funded first. In comparing the agencies request to the recommendation, you will find that the Governor has been very selective in what he is recommending for new spending.

The economy is growing. With this will come additional state revenue. However, the Governor believes that we must remain vigilant in our effort to safeguard public funds. While there are real pressing needs that must be addressed across state government, now is not the time for unbridled growth in spending.

FY 2012 Summary

| | At Sine Die (April 7) | Governor's Recommendation | Difference |
|---------------------------|--------------------------|------------------------------|--------------|
| Beginning Balance | 39.4 | 68.7 | 29.3 |
| Reappropriations | 0.0 | 1.3 | 1.3 |
| Revenue Forecast | 2,521.5 | 2,552.6 | 31.1 |
| 3% Budget Cap | -91.5 | 0.0 | 91.5 |
| 2011 Legislation | 24.7 | 0.0 | -24.7 |
| Transfers to General Fund | 38.0 | 38.0 | 0.0 |
| Appropriations | -2,529.0 | -2,529.0 | 0.0 |
| Deficiency Warrants | 0.0 | -4.2 | -4.2 |
| Supplementals | <u>0.0</u> | <u>-23.9</u> | <u>-23.9</u> |
| Ending Balance | 3.1 | 103.5 | 100.4 |

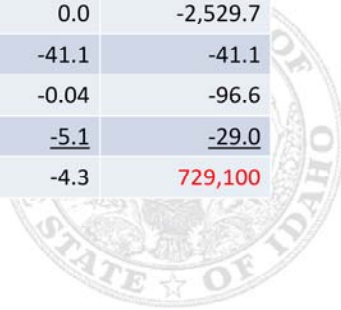


In conclusion, let me summarize quickly the Governor's recommendation with two charts.

This chart shows the current fiscal year, and due to your hard work last session we anticipate ending the year with a healthy carryover in to FY 2013.

FY 2013 Summary

| | Ongoing | One-Time | Total |
|------------------------------|--------------|-------------|--------------|
| Beginning Balance | 0.0 | 103.5 | 103.5 |
| Revenue Forecast | 2,700.3 | 0.0 | 2,700.3 |
| Tax Relief | -45.0 | 0.0 | -45.0 |
| Rainy Day Fund Transfers | 0 | -60.0 | -60.0 |
| Transfer to Const. Def. Fund | 0 | -1.5 | -1.5 |
| Projected Base | -2,529.7 | 0.0 | -2,529.7 |
| Surplus Eliminator (3% CEC) | 0.0 | -41.1 | -41.1 |
| Maintenance Items | -96.6 | -0.04 | -96.6 |
| Line Items | <u>-23.9</u> | <u>-5.1</u> | <u>-29.0</u> |
| Ending Balance | 5.0 | -4.3 | 729,100 |



In FY 2013, the Governor's recommendation accounts for those items most essential to the continued operation of state government, transfers to the state rainy day funds and tax relief.

Thank You

- Sign up for monthly updates on state revenues by sending an email to:

info@dfm.idaho.gov

- Get regular updates from the Governor at:

gov.idaho.gov

- Get additional budget information at:

dfm.idaho.gov

